

General Information Letter: Application to mail order software company.

February 19, 1998

Dear:

This is in response to your letter of January 30, 1998, which was received by the Office of Chief Counsel on February 17, 1998. Department rules require that the Department issue two types of letter rulings, private letter rulings (**PLRs**) and general information letters (**GILs**). For your general information we have enclosed a copy of 2 *Ill. Adm. Code 1200* regarding letter rulings and other information issued by the Department.

Although you have specifically requested a **PLR**, the nature of your questions require that we respond with a **GIL**. **GILs** are designed to provide background information on specific topics, however, **GILs** are not rulings that are binding on the Department, but **PLRs** are binding on the Department.

In your letter you inquire about the Illinois income and sales tax return filing requirements of your client, xx&x xxxxxxxx xxxx. for tax years ending after 3/28/98. After that date, it is our understanding that xx&x xxxxxxxx will be conducting business under a different manner of operations. Your letter states in part as follows:

Facts

xx&x is a retailer of tangible personal property. In the past, xx&x has generated sales through a variety of different business activities. xx&x operated several retail stores and sales offices located throughout the United States and Canada, including Illinois. xx&x has also employed direct salespeople who solicited sales from corporate, government and educational organizations. These salespeople were based throughout the country, including

Illinois, and made sales calls to companies in your state. In addition, xx&x sells its products via mail order and solicits mail order sales primarily through catalogs and other promotional materials which are sent directly to consumers. Mail order sales are also accepted through xx&x's web page. All items sold through the mail order division are delivered to customers by common carrier. All orders are accepted at its Corporate headquarters located in another state and are delivered from inventory stored in a warehouse also in another state. xx&x is currently registered with the Department for both corporate income tax and retailers' occupation/use tax purposes.

xx&x has recently announced plans to close numerous retail stores throughout the country. As a result, xx&x will close all retail stores that operate in Illinois. One of the two stores has a lease that runs through August 7, 2000; another store has a lease that runs through August 31, 2000. xx&x is currently negotiating with the landlord of the stores scheduled for closing to reach a mutually acceptable settlement with respect to the lease termination. xx&x may sublease the vacated stores if it is unable to reach a settlement agreement with the landlord. If settlement agreements are reached,

xx&x plans to immediately pay the landlord the amount agreed upon to terminate the lease.

Prior to closure of its retail stores, xx&x sold its direct sales division effective May 13, 1996. As a result, xx&x no longer operates sales offices (other than its Corporate headquarters in another state) or employs direct salespeople and has not employed direct salespeople or independent representatives since May of 1996. Thus, with the closure of its retail stores, xx&x no longer has a physical presence in Illinois.

Due to the tremendous administrative burden associated with filing retailer's occupation/use tax and corporate income tax returns, xx&x would like to formally withdraw from Illinois as it will no longer be conducting business through in-state retail outlets or in-state salespersons.

xx&x will continue to operate its mail order business and anticipates that sales into Illinois may exceed \$100,000 on an annual basis. However, these mail order sales will be solicited only through catalogs, similar promotional mailings, or via xx&x's web page. All mail order sales will be delivered via common carrier or electronically via the Internet.

Conclusion

xx&x will no longer have nexus in Illinois after the closure of its retail stores in March, 1998. Therefore, xx&x will terminate its retailer's occupation/use tax registration with Illinois and will stop collecting retailer's occupation/use tax as of March 28, 1998. xx&x's final retailer's occupation/use tax return will be filed in April, 1998. In addition, xx&x will file its final income tax return with Illinois for its fiscal year ending in March, 1998. xx&x will file a formal withdrawal application with Illinois prior to March 28, 1998 (its fiscal year end date).

With the closure of its retail stores, xx&x has no physical presence in the form of in-state tangible personal property, inventory, employees, independent contractors, real property, business offices or subsidiaries. xx&x will continue to solicit sales in Illinois via catalogs and other direct mail. Customers may also order products by accessing xx&x's web page. However, under *Quill Corp. v. North Dakota*, 112 S. Ct. 1904 (1992), these activities are not nexus creating activities and under *Wisconsin Department of Revenue v. William Wrigley, Jr., Co.*, 112 S. Ct. 2447 (1992), these activities are protected. Thus, Illinois may not impose its taxes or a duty to collect taxes upon xx&x after xx&x terminates its in-state physical presence.

In your letter, you are questioning whether your company has the requisite connection (nexus) with the State of Illinois, to be subject to Illinois income taxation. The determination of nexus is extremely fact-dependent. As a result, we decline to issue private letter rulings on the issue of whether a particular taxpayer has nexus with the State of Illinois. Such a determination may only be made in the context of an audit where the Department's auditor would have access to all relevant facts and circumstances.

Under Section 201 of the Illinois Income Tax Act, a tax measured by net income is imposed on a corporation for the privilege of earning or receiving income in this State. However, out-of-state ("foreign") corporations whose only activity within Illinois consists of the mere solicitation of orders for items of tangible personal property, which orders are accepted or rejected outside of Illinois, and if accepted are filled from inventories maintained outside of Illinois by shipment or delivery from those inventories to the customer within

Illinois, are not subject to Illinois income tax because of the application of Public Law 86-272.

If a corporation exceeds this "mere solicitation" standard in Illinois, it loses its immunity and will be liable for income and the additional replacement income tax for the entire year. The business income would be apportioned to Illinois under Section 304 of the Illinois Income Tax Act pursuant to a three factor formula based upon the corporation's Illinois property, payroll and sales (with the sales factor double-weighted) versus the total property, payroll and sales everywhere.

The foregoing constitutes only a general statement of Public Law 86-272 immunity from Illinois income tax and replacement income tax. The immunity is narrowly construed and can be easily forfeited. Whether a corporation's conduct exceeds the "mere solicitation" standard depends on the facts in each particular case. Note, however, that continuing to hold a leasehold interest in real property in Illinois exceeds the "mere solicitation" standard.

You should be aware that Section 502(a)(2) of the Illinois Income Tax Act requires that a corporation which is authorized to do business in this State, and is required to file a Federal income tax return will be required to file an Illinois income tax return regardless of whether the corporation is liable for Illinois income tax. Based upon the information contained in your letter, it appears that xx&x will be required to file an Illinois income tax return so long as it is required to file a federal income tax return.

A copy of your correspondence has been referred to Mr. Karl Betz, of the Department's Sales Tax Division of the Chief Counsel's office for a reply regarding the non-income tax issues raised therein.

Very truly yours,

Jackson E. Donley
Associate Counsel